

Confidential Facts - Round 1 - Biomassive

Biomassive views itself as an environmental steward, and is shocked and offended by the citizen suit. Biomassive would like to have the suit dismissed, but recognizes that it might end up in lengthy, costly litigation. Thus, it is willing to try to work something out with the citizens.

1. Damages

Biomassive thinks that the citizens may get a sympathetic jury to believe the sooty deposits came from the plant, but because it has recently spent \$20 million to upgrade its equipment at its Ripon facility, there have been no instances of sooty deposits since the facility upgrades. Biomassive thinks the citizens will have difficulty establishing a continuing permit violation at the Ripon facility and this may weaken the citizens' Clean Air Act claim. In addition, it thinks the citizens' alleged property damages are overstated.

Biomassive is willing to give or take some dollars on the property or health issues to get a global settlement. It will spend up to the total of \$5 million to resolve the all money issues in the dispute with the neighbors, but obviously it would prefer to spend as little as possible. Litigating the case through trial could cost up to \$5 million, and it will pay that amount for the certainty of a settlement.

A. Property Value

Biomassive hired an environmental consulting firm that told it that some - but likely not all - of the sooty deposits alleged could have come from neighborhood fireplaces. And the fireplaces would likely have not been a source of sooty deposits in the summer, when the soot was the worst. Despite its experts' opinion, Biomassive does not believe its facility caused the soot problem, and it certainly will not admit that it has any problems now with its new, upgraded facility. But it knows this testimony will not help its case. It plans to seek a second opinion if the matter goes to trial. This would mean more costly experts.

Biomassive's property appraiser estimates that the houses in the neighborhood diminished in value approximately \$75,000 each in the last three years. He says this is due to a number of factors, the most dominant of which is the poor real estate market. In his opinion, the sooty deposits the neighbors describe, and the negative press about the problem, could have contributed between \$5,000 and \$10,000 of this loss in value.

To rid itself of the troubling soot allegations (and buy some good press) Biomassive will agree to pay up to \$350,000 towards re-painting the neighbors' homes and vehicles. In the alternative, a lump-sum payment of between \$20,000 and \$300,000 would be reasonable.

B. Health Effects

On the risk of future health injuries, Biomassive is more concerned. The company does not want to have to defend future claims that might arise years from now, and is willing to spend money now - with its \$5 million bottom line in mind - in order to obtain releases of future liability from the citizens. Obviously, if it settles for as little as \$20,000 on the property value, it can spend more on the health issues.

Floyd Hawken's kidney disease is also an issue for Biomassive. Even though Biomassive's expert witness will testify that the kidney failure could not have been caused by Biomassive's emissions, the company is concerned that a jury could be sympathetic to Hawken and his family and be more inclined to believe the testimony of his doctor, and therefore return a large award. Ultimately, Biomassive does not care how much money is allocated to Hawken versus the other neighbors, as long as it gets a complete release from them all for current and future health issues.

Citizen suit penalties under the Clean Air Act are also a concern for Biomassive. The company does not want further bad publicity. In fact, Biomassive would strongly prefer that no portion of its monetary payment to be characterized as a "penalty" under the settlement, because it hopes to be able to deduct the payment as a business expense. This will be an issue for Biomassive's tax lawyers to handle separately.

2. Injunction

Biomassive is very concerned that citizens' injunctive requests are based on misinformation about how it runs its business. Biomassive already has in place operational guidelines for companies making deliveries requiring that loads of incoming waste be covered, and attempts to limit deliveries to 10 a.m. to 4 p.m. Biomassive is adamant that the terms of any injunction not significantly impair its operational flexibility, and in particular its ability to extend delivery hours as desired during peak energy demand. It therefore intends to push back hard on any demand that limits its hours of operation or operational methods. But as a tradeoff for a smaller cash payment, company officials are willing to agree to limit the total number of truck deliveries per day.

Biomassive views urban waste as a plentiful source of cheap or free fuel, and will not agree to completely eliminate urban waste from its fuel supply. It would, however, agree to only burn a specified percentage of urban fuel at any given time, blending it with the cleaner-burning agricultural products. It would also be willing to fund an on-site inspector to perform random inspections of loads of urban wood waste delivered to the Ripon facility. That inspector would have authority to reject any loads that contain non-wood materials such as plastic and non-permitted fuels such as painted or chemically treated wood.

The company does not want to publish its monitoring data on the internet in real time, but it also knows that refusing to agree to such a term would make it appear as if it has something to hide. As a last resort, the company will agree to place its monitoring data on the internet, if it is

satisfied with the other terms obtained from the citizens.

Confidential Facts Round 2 – Biomassive, Inc.

Biomassive's overarching goals for early settlement negotiations with the ARB are 1) pay as little as possible, because the company believes it has already paid to the locals, for private settlements, and for facility upgrades; 2) minimize payments characterized as "penalties" and instead pay for things that might be tax deductible¹; and 3) maximize Supplemental Environmental Projects (SEPs) that benefit the company's business plan and public relations.

The Local Agency Settlement Agreements

Biomassive will argue that its settlement agreements with the local air districts negate any claim by the ARB. If a favorable settlement cannot be reached with ARB, Biomassive will take its chances in court and argue for a complete victory. Biomassive believes that the settlement agreements bind the entire state and disagrees with ARB's stated view that a judge would find these documents to be shams.

1. Penalty

Biomassive officials were shocked to see that its monitoring data for June-September showed potential permit violations nearly every day. On some days Biomassive exceeded both the three hour and twenty-four hour permit limits for criteria pollutants. The state penalty statute provides for a range of penalties and requires the agency or the factfinder to consider as appropriate the statutory factors in setting the penalty.

The penalty factors are: (1) The extent of harm caused by the violation; (2) The nature and persistence of the violation; (3) The length of time over which the violation occurs; (4) The frequency of past violations; (4) The record of maintenance; (5) The unproven or innovative nature of the control equipment; (6) Any action taken by the person including the nature, extent, and time of response of any cleanup and construction undertaken, to mitigate the violation; (7) The financial burden on the defendant; and (8) Any other circumstances the court deems relevant. Cal. Health & Saf. Code, § 42400.8.

The penalties are significant, ranging from \$25,000 to \$75,000 per day depending on whether the agency can show the violation was negligent, knowing, or intentional. See generally Cal. Health & Saf. Code, §§ 42400.1-42400.3.

¹It will be up to Biomassive's tax accountants to determine tax deductibility, at a later date. You should not be concerned with ultimate tax status for purposes of this competition. Penalties are not tax deductible, and may even survive a bankruptcy. Minimize penalties to the extent possible.

Biomassive expects that ARB will assert the maximum statutory penalty of \$75,000/day for 122 days, or \$9,150,000.² In response, Biomassive will argue factors in mitigation, including its belief that it helped prevent blackouts during the energy crisis. It will seek the lowest penalties. Biomassive also believes its internal audit and self-disclosure of the tampering are mitigating factors. See <http://www.calepa.ca.gov/Enforcement/Policy/VolDisclosure.pdf>.

Biomassive believes that the company's role in the violations was negligent at worst, the result of employee misconduct. All of the employees involved in tampering have been terminated. Biomassive has paid fines to the local air districts, and spent \$20 million on facility upgrades. In light of all this, Biomassive thinks it should pay no fine at all to the state. But it knows that the state will want some portion of the payment to be characterized as a fine, and Biomassive is willing to negotiate. Biomassive officials think a payment of \$3 to \$6 million as a "penalty" would be a success in early negotiations, and is loathe to go higher, but will do so if absolutely necessary to close a deal that has other good components benefitting Biomassive. Other payments should be made as SEPs or further facility upgrades, which will make for much better press for the company.

2. Economic Benefit

Biomassive expects ARB will want to discuss disgorgement of its energy profits. Biomassive views this as just another way to penalize the company. Its actual overall profits have been low – the agricultural industry has suffered in recent years from international competition and rising labor and transportation costs, particularly fuel costs. While the company made money from selling energy, overall it suffered losses in 2007. Any repayment of "economic benefit" is simply economic punishment for the company.

Biomassive is willing to give up some of its energy profits, but only if doing so reduces the amount of the "penalty" Biomassive pays, above, with the hope that it can find a favorable tax treatment for the payment. Biomassive also thinks that ARB is overstating the amounts of its profits earned at \$17 to \$24 million. Biomassive thinks at trial it will be able to show its actual profits from energy for 2006 at about \$15 million. It believes it is worth going to trial to avoid paying that amount, but it is worth settling if the disgorgement amount can be reduced to an amount no more than half that number.

3. SEPs

Biomassive particularly wants to discuss various SEPs in lieu of payment of at least a part of any penalty. It understands there are criteria restricting the type of proposals eligible as SEPs, but Biomassive would look most favorably on SEPs meeting those criteria that would also benefit

²ARB could seek additional penalties for violations of the three hour limits (up to 8/day) but proving the actual number of three hour violations at trial will be extremely difficult, given the available data.

aspects of its business organization and image.

SEPs that Biomassive would prefer include upgrading its truck fleet to modern, cleaner-burning engines; upgrading its diesel agricultural equipment, such as generators; continuing with further facility upgrades at its co-generation plants. Biomassive is not interested in SEPs that come with ongoing administrative or labor costs. Biomassive is also dead set against paying for any SEPs that will fund future environmental investigations or prosecutions of Biomassive or any other California businesses.

Biomassive has thousands of acres of Bay-Delta agricultural islands. The agricultural tracts are currently being farmed by Biomassive, but it knows that in the long term, farming in the Delta will continue to be reduced as the lands erode and Delta water supplies continue to diminish. Because of its long-time support for Waterfowl Forever, Biomassive is willing to consider donating up to 2000 acres of agricultural land tracts in the Bay-Delta for wildlife preserve land, as long as those lands would be open for duck hunting, at least to Biomassive officials. Biomassive also wants to retain the water rights to the property, for possible sale in the future. Additionally, Biomassive must retain the right to select which specific acres of property it is willing to put into the wildlife preserve. Biomassive will want credit against the penalty and disgorgement claims for the value of the property it donates. The commercial value of property in the Delta is presently about \$25,000 per acre, apart from the high ecological value of undeveloped land in the Delta.

4. Oversight

Biomassive expects the regulators will want to recoup the costs of their investigation. In the overall picture, this amount of money is negligible, but Biomassive is annoyed by all the attention it has received in recent months, and will not pay more than \$250,000 for the agency's oversight costs.